INDEX

	Page
Opinions below	1
Jurisdiction	2
Question presented	2
Statutes and regulations involved	2
Statement	2
Specification of errors to be urged	4
Reasons for granting the writ	5
Appendix (Statutes and regulations)	11

CITATIONS

Cases:	
Alexander Sprunt & Son v. *Commissioner*, 64 F. (2d) 424	5
Atlantic Bank & Trust Co. v. *Commissioner*, 59 F. (2d) 363	5
Becker v. *United States*, 21 F. (2d) 1003	5, 7
Burnet v. *Houston*, 283 U.S. 223	7
Darcy v. *Commissioner*, 66 F. (2d) 581, certiorari denied, 290 U.S. 705	6
Houston v. *Commissioner*, 53 F. (2d) 445	8
Lightsey v. *Commissioner*, 63 F. (2d) 254	5
Matern v. *Commissioner*, 61 F. (2d) 663	5
Saxman Coal & Coke Co. v. *Commissioner*, 43 F. (2d) 556	5
Thom v. *Burnet*, 55 F. (2d) 1039	8
Underwood v. *Commissioner*, 56 F. (2d) 67	8
Williams v. *Commissioner*, 45 F. (2d) 61	5
Statutes:	
Revenue Act of 1926, c. 27, 44 Stat. 9:	
Sec. 1003 (U.S.C.App., Title 26, Sec. 1226)	11
Revenue Act of 1928, c. 852, 45 Stat. 791, 807, 808, 815, 818:	
Sec. 51 (a)	11
Sec. 54 (a)	11
Sec. 111	12
Sec. 113	12
Miscellaneous:	
Regulations 74, Art. 58	13

79517—34

In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 289

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

WALTER W. TAYLOR

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

The Solicitor General on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Second Circuit entered in the above cause on May 18, 1934, reversing the decision of the Board of Tax Appeals and remanding the cause for further proceedings in conformity with the opinion.

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 12) is unreported. The opinion of the Circuit Court of Appeals (R. 33) is reported in 70 F. (2d) 619.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on May 18, 1934 (R. 36). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the Circuit Court of Appeals erred in remanding this case to the Board of Tax Appeals for a new hearing on the ground that the Commissioner's determination of the amount of income was incorrect, although the taxpayer had failed to prove facts from which a correct determination could be made.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set out in the Appendix, *infra*, pp. 11–13.

STATEMENT

The facts as found by the Board of Tax Appeals (R. 13–16) may be summarized as follows:

Shortly before August 1927 the taxpayer secured options to purchase for specified amounts either the stocks or properties of four public utility companies in Vermont (R. 13). Thereafter, he exercised the options, purchasing the stocks of three of the companies and the assets of the fourth. He then organized a separate corporation to which he conveyed the assets of the fourth company, re-

ceiving its stock in exchange. On October 13, 1927, he organized a holding company to which he conveyed the stocks of the four operating companies and received in exchange all the stock of the holding company, being 1,000 shares of preferred stock without par value, entitled to cumulative dividends of $6 per share and callable at $105 per share; 2,500 shares of Class A no par common, callable at $35 per share; and 5,000 shares of Class B no par common. (R. 14.)

In May 1928 the holding company sold the stocks of these four operating companies for $194,930.16. Thereafter, in the year 1928, the taxpayer sold his preferred stock in the holding company to that company for $99,000. In his income tax return the taxpayer reported the sale of this preferred stock, assigning $96,030, the original aggregate cost of the properties, as the cost of the preferred stock, and $99,000 as the sales price, with resulting profit of $2,970. (R. 14.) When the taxpayer transferred the stocks of the utility companies to the holding company, receiving in exchange therefor all the stock of the latter company, the transaction came under the reorganization provisions of the Revenue Act of 1926, and resulted in no tax at that time. Therefore, the basis for determining gain or loss with respect to the sale of stock of the holding company would be the same as the stock exchanged therefor. The taxpayer, however, did not sell all the stock but only the pre-

ferred, making it necessary to ascertain the basis for determining gain on sale of the preferred stock. (R. 14–15.)

The Commissioner determined the cost to the taxpayer of the holding company's preferred stock to be $\frac{99,000}{194,930.17}$ of $96,030 or $48,771.16, the balance of the $96,030 representing the cost of the common stock (R. 15). This cost, deducted from the admitted sale price, $99,000, produced a profit of $50,228.84 (R. 16).

Upon appeal to the Board of Tax Appeals, the Commissioner's determination was sustained (R. 18).

The Circuit Court of Appeals reversed the decision of the Board of Tax Appeals and remanded the cause to the Board for a new hearing on the ground that the Commissioner's determination of cost basis was wrong, although the taxpayer had failed to introduce evidence to show the correct basis.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the taxpayer had discharged the burden of proof resting upon him merely by showing that the Commissioner's determination was wrong without proof of facts from which a correct determination could be made.

2. In remanding the cause to the Board of Tax Appeals for further proceedings in conformity with the opinion of the Circuit Court of Appeals.

3. In holding that the Commissioner's determination was plainly erroneous.

4. In reversing the order of the Board of Tax Appeals sustaining the Commissioner's determination.

REASONS FOR GRANTING THE WRIT

1. The instant case, in holding that the taxpayer was only required to show that the Commissioner's determination of cost basis for the preferred stock was incorrect, conflicts in principle with the cases which have established the rule that the burden is on the taxpayer to show the correct amount of the tax in order to have the Commissioner's determination set aside. *Williams* v. *Commissioner*, 45 F. (2d) 61 (C.C.A. 5th); *Becker* v. *United States*, 21 F. (2d) 1003 (C.C.A. 5th); *Saxman Coal & Coke Co.* v. *Commissioner*, 43 F. (2d) 556 (C.C.A. 3d); *Alexander Sprunt & Son* v. *Commissioner*, 64 F. (2d) 424 (C.C.A. 4th); *Atlantic Bank & Trust Co.* v. *Commissioner*, 59 F. (2d) 363 (C.C.A. 4th); *Lightsey* v. *Commissioner*, 63 F. (2d) 254 (C.C.A. 4th); *Matern* v. *Commissioner*, 61 F. (2d) 663 (C.C.A. 9th). The court below, while regarding certain of these cases as distinguishable, conceded that "the cases are not all in accord" and that "at least the law is not settled." 70 F. (2d) 619, 621.

The dissenting judge wrote no opinion, but it seems probable that his dissent was based upon the

foregoing rule, which he had announced in an earlier case, *Darcy* v. *Commissioner*, 66 F. (2d) 581, 585 (C.C.A. 2d), certiorari denied, 290 U.S. 705, as follows:

> The burden is upon the petitioners to show the correct amount of the tax in order to show that the commissioner's determination was wrong. Compare *Burnet* v. *Houston*, 283 U.S. 223, 228, 51 S.Ct. 413, 75 L. Ed. 991; *Reinecke* v. *Spalding*, 280 U.S. 227, 232, 233, 50 S.Ct. 96, 74 L. Ed. 385. * * *

2. The opinion below draws a distinction between suits to recover taxes paid and proceedings to review assessments; also between cases involving deductions and cases relating to income items. The court held that the taxpayer does not have the burden of proving the correct amount of tax when the purpose of the suit is to review assessments of income items, as in the present case. We submit that such a refinement of the rule relating to the burden of proof is unwarranted and that no distinction should be drawn between deductions and income, or between suits for refund and proceedings before the Board of Tax Appeals. It is believed that in all cases the burden is on the taxpayer to show the proper amount of tax. This seems to follow from the proposition that from the beginning the taxpayer is required to show the correct amount of tax and the facts upon which the tax is based. See Sections 51 (a) and 54 (a) of the Revenue Act of 1928, *infra*, p. 11. This burden must per-

sist when the matter of his tax liability is presented to the Board of Tax Appeals for review. Moreover, the fact that a deficiency determined by the Commissioner is too great does not mean that the whole is erroneous; and the taxpayer should be required to show in a proceeding before the Board how much of the deficiency is not due or that no deficiency is owing, for the same reason as in a suit for refund he must show that he is not liable for the whole or a part of the amount collected. In *Becker* v. *United States, supra,* a suit was brought by the United States to recover the amount of an assessment which the taxpayer claimed to be erroneous. The court held that the taxpayer must show how much should be disallowed, since, upon proof that the assessment should be reduced by any particular amount, the Government would still be entitled to recover the remainder.

3. If, as we contend, the principle that the taxpayer bears the burden of proof applies to the instant case, then the Board properly affirmed the Commissioner's determination on the ground that the taxpayer had not proved that the amount to be allocated to the preferred stock was any different from that determined by the Commissioner, and consequently there was no error of law in the Board's decision. Compare *Burnet* v. *Houston,* 283 U.S. 223. The Circuit Courts of Appeals have no power to remand a case unless the decision of the Board is not in accordance with law. Revenue

Act of 1926, Section 1003 (b), *infra*, p. 11. It has been so held in *Houston* v. *Commissioner*, 53 F. (2d) 445 (C.C.A. 3d) and *Thom* v. *Burnet*, 55 F. (2d) 1039 (App. D.C.); and the decision of the Circuit Court of Appeals in remanding the instant case to the Board for a new hearing is in conflict with those cases. But see *Underwood* v. *Commissioner*, 56 F. (2d) 67 (C.C.A. 4th), and authorities there cited.

4. We submit that the court below erred in holding that the Commissioner's determination of the allocated cost of the holding company's preferred stock was plainly erroneous. That conclusion appears to have been based upon the ground that his determination necessarily assumed that the preferred stock was worth only some $49,000 out of a total value of approximately $96,000 for the preferred and common stocks together. Such is not the case. The $48,771.16 assigned by the Commissioner to the preferred stock did not represent its value at date of acquisition by the taxpayer or at any other date, but only the proportionate part of the original cost to the taxpayer of the operating companies which should be allocated to the holding company's preferred stock. Even if the amounts used by the Commissioner in making the allocation, based upon conditions some eight months after the date for valuation, were remote in time, his result nevertheless may have been correct. The basic cost of $96,030 comprised the aggregate price of the original properties as fixed in the options granted

prior to August 1927 (R. 13). The holding company to which the properties were transferred was not organized and the preferred stock was not issued until October 13, 1927, at least two or three months after the date of the options. It is difficult to believe that the preferred and common shares issued by the holding company in connection with the reorganization were not worth more than $96,030 at date of issuance. Certainly such a merger in the fall of 1927 of four small utility companies, with resultant economies of operation and other advantages of combination, would tend to create a total value for the shares of the new company far higher than the sum of the values of the stocks or properties of the four original companies prior to the merger. It would accordingly follow that the value of the preferred and common shares of the holding company at date of issuance was substantially in excess of $96,030. At least, there is nothing to compel the conclusion that they were worth no more.

5. The effect of the decision below is to impose upon the Commissioner the duty of proving a new proposed assessment—a difficult proposition, since the facts with respect to the valuation of assets and the income of the operating companies, which the court suggested as a datum to arrive at the correct basis of the preferred stock, are peculiarly within the knowledge of the taxpayer and his associates. Conceivably, as a result of the court's decision, the Commissioner might have to make a series of

subsequent determinations if the taxpayer shows that each one is wrong without showing the correct amount—clearly an undesirable situation from the standpoint of efficient tax administration. The question thus presented by this case is important not only for that reason but also because the decision of the court below is likely to produce uncertainty and confusion with respect to the proper procedure in cases remanded to the Board.

Wherefore it is respectfully submitted that this petition should be granted.

J. CRAWFORD BIGGS,
Solicitor General.

AUGUST 1934.

APPENDIX

Revenue Act of 1926, c. 27, 44 Stat. 9:

> SEC. 1003. (a) The Circuit Courts of Appeals and the Court of Appeals of the District of Columbia shall have exclusive jurisdiction to review the decisions of the Board (except as provided in section 239 of the Judicial Code, as amended); and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari, in the manner provided in Section 240 of the Judicial Code, as amended.
>
> (b) Upon such review, such courts shall have power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require.
>
> (U.S.C. App., Title 26, Sec. 1226.)

Revenue Act of 1928, c. 852, 45 Stat. 791, 807, 808, 815, 818:

> SEC. 51. INDIVIDUAL RETURNS.
>
> (a) *Requirement.*—The following individuals shall each make under oath a return stating specifically the items of his gross income and the deductions and credits allowed under this title—
>
> * * * * *
>
> SEC. 54. RECORDS AND SPECIAL RETURNS.—(a) *By taxpayer.*—Every person liable to

any tax imposed by this title or for the collection thereof, shall keep such records, render under oath such statements, make such returns, and comply with such rules and regulations, as the Commissioner, with the approval of the Secretary, may from time to time prescribe.

* * * * *

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.—(a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in section 113, and the loss shall be the excess of such basis over the amount realized.

* * * * *

(d) *Recognition of gain or loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

* * * * *

SEC. 113. BASIS FOR DETERMINING GAIN OR LOSS.—(a) *Property acquired after February 28, 1913.*—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; except that—

* * * * *

(6) *Tax-Free Exchanges Generally.*—If the property was acquired upon an exchange described in section 112 (b) to (e), inclusive, the basis shall be the same as in the case of the property exchanged, decreased in the amount of any money received by the tax-

payer and increased in the amount of gain or decreased in the amount of loss to the taxpayer that was recognized upon such exchange under the law applicable to the year in which the exchange was made. * * *

Treasury Regulations 74:

ART. 58. *Sale of stock and rights.*—* * * Where common stock is received as a bonus with the purchase of preferred stock or bonds, the total purchase price shall be fairly apportioned between such common stock and the securities purchased for the purpose of determining the portion of the cost attributable to each class of stock or securities, but if that should be impracticable in any case, no profit on any subsequent sale of any part of the stock or securities will be realized until out of the proceeds of sales shall have been recovered the total cost.

* * * * *

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